Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington D.C. 20554

In the Matter of:	)	
	)	
Implementation of the Local Competition Provisions in the Telecommunications Act of 1996	)	CC Docket No. 96-98
	)	
	)	
Intercarrier Compensation for ISP-Bound Traffic	)	CC Docket No. 99-68

OPPOSITION OF BELLSOUTH TELECOMMUNICATIONS, INC., SBC COMMUNICATIONS INC., THE VERIZON TELEPHONE COMPANIES, AND THE UNITED STATES TELECOM ASSOCIATION TO THE PETITION OF CORE COMMUNICATIONS, INC. FOR STAY PENDING JUDICIAL REVIEW

INTRODUCTION AND SUMMARY

In its *Order on Remand*,[1] the Commission determined that the payment of reciprocal compensation for Internet-bound traffic had "created opportunities for regulatory arbitrage and distorted the economic incentives related to competitive entry in the local exchange and exchange access markets." *Id.* ¶ 2. CLECs were not competing based on their "ability to provide efficient and quality service to ISPs"; rather, they used ISP customers as a means "to reap an intercarrier compensation windfall." *Id.* ¶¶ 21, 86. The Commission concluded that this regime discouraged CLECs from providing local voice service, and was fundamentally incompatible with the pro-competitive goals of the 1996 Act. *Id.* ¶ 21.

[1] Order on Remand and Report and Order, *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Intercarrier Compensation for ISP-Bound Traffic*, FCC 01-131, CC Docket Nos. 96-98 & 99-68 (rel. Apr. 27, 2001) ("*Order on Remand*").

For these reasons, the Commission determined that "a bill and keep approach to recovering the costs of delivering ISP-bound traffic is likely to be more economically efficient" than establishing a reciprocal compensation regime. *Id.* ¶ 67; *see id.* ¶ 6. The Commission thus created "an interim compensation mechanism" to move toward that goal where state regulatory commissions previously had imposed a reciprocal compensation requirement. *Id.* ¶ 66. That regime — under which all carriers are free to recover their costs from their own customers just as incumbents already must — is designed to "produce meaningful reductions in intercarrier payments for ISP-bound traffic" and to impose "a standstill on any expansion of the old compensation regime." *Id.* ¶¶ 81, 84.

Now, after waiting more than a month to seek relief for injuries that it claims threaten its competitive viability, a single carrier, Core Communications, Inc. ("CoreTel"), asks the Commission to stay its order so that CoreTel can expand its exploitation of the very regulatory arbitrage that the Commission has concluded is harming competition. A stay would squarely conflict with the Commission's determination that allowing CLECs "to expand into new markets using the very intercarrier compensation mechanisms that have led to the existing problems *would exacerbate the market problems we seek to ameliorate*." *Id.* ¶ 81 (emphasis added).

Indeed, CoreTel's arguments are utterly without merit. There is no dispute that the Commission has authority to establish transition plans such as the one at issue here. It was the recipients of reciprocal compensation that urged the Commission to establish a transition plan in the first place. Nor can there be any doubt that the Commission is entitled to great deference in determining where to draw the lines in fashioning such a plan. Again, the recipients of reciprocal compensation generally have praised the plan adopted here as establishing a reasonable balance. Consequently, CoreTel is left to argue weakly that the Commission

somehow abused its discretion in drawing the line in a way that "discriminates" against CoreTel. That is flatly wrong.

The reality is that the Commission established an even-handed transition plan that applies equally to all similarly situated carriers — those who previously were entitled to receive reciprocal compensation in particular states. Insofar as CoreTel wants to expand into new markets, it is differently situated from CLECs that have already entered contracts with customers and are providing service to ISPs in particular markets. Because of these differences, CoreTel is, in effect, demanding *preferential* treatment. While the Commission established a transition to phase *down* payments to these other carriers, CoreTel effectively claims that the Commission must phase *up* payments to it. Moreover, CoreTel knew that the reciprocal compensation "gravy train" (as one analyst termed it) was undergoing review and by all accounts was about to run out of track. Nonetheless, it gambled that the inefficient arbitrage opportunity would last long enough for it to reap additional rewards from that boondoggle. The fact that it "sought to game the existing rules, and lost, does not mean" that the Commission acted arbitrarily here. *Global NAPs, Inc. v. FCC*, 247 F.3d 252, 260 (D.C. Cir. 2001).

That is especially true in this case, because precedent establishes that the Commission had considerable discretion in fashioning a transition mechanism to respond to the "need for immediate action . . . to eliminate arbitrage opportunities." *Order on Remand* ¶ 7. Under that precedent, including recent on-point D.C. Circuit decisions, it was an entirely reasonable exercise of that discretion to create a bright-line rule limiting the compensation available to CLECs based on the services they were actually providing to ISPs as of the adoption of the *Order on Remand*. As discussed further below, moreover, CoreTel's procedural arguments are contrary to established law.

CoreTel's arguments on the balance of equities similarly lack substance. As an initial matter, CoreTel is not entitled to skim off uneconomic subsidy payments to begin with, and it remains free to recover any costs it incurs from its own customers, just as incumbents already must. Consequently, CoreTel simply cannot show any cognizable harm.

In contrast, the Commission has expressly found that the payment of reciprocal compensation on Internet-bound calls is distorting competition. Consequently, the Commission has determined that the public interest strongly supports phasing out reciprocal compensation for Internet-bound traffic as quickly as reasonably possible and, in the interim, preventing its expansion into new markets and restricting the payment of such compensation on increased traffic. Further, CoreTel's argument is compromised both by its failure to assert its claim promptly and by the enormous harm that a stay would inflict on incumbent LECs.

ARGUMENT

CoreTel's stay request fails both on the law and on the balance of equities. We address each in turn.

1. CoreTel raises no challenge to the Commission's conclusion that payment of "reciprocal compensation for Internet-bound traffic distorts the development of competitive markets," because the "windfall" such compensation offered CLECs led to "classic regulatory arbitrage." *Order on Remand* ¶¶ 21, 29, 70. Accordingly there is no dispute that the conduct in which CoreTel seeks to engage — relying on reciprocal compensation payments to provide below-cost service to ISPs (*see* Petition at 17) — is contrary to the 1996 Act's central goal of enhancing competition. As the Commission has determined, conduct of this sort "undermines the operation of competitive markets" (*id.* ¶ 71). Indeed, the stay that CoreTel seeks would defeat the very goals enunciated in the *Order on Remand.* Instead of moving rapidly to end

inefficient entry and regulatory arbitrage, a stay of the new-market and growth-cap restrictions would *expand* those anticompetitive tactics to new carriers and new opportunities. The stay request is thus fundamentally irreconcilable with the principles adopted in the *Order on Remand*, and it should be rejected for that reason alone.

Nor is there merit to CoreTel's claim that the interim compensation regime "discriminates" against it and in favor of carriers that were serving ISP customers at the time of the Commission's order. CoreTel will suffer no cognizable discrimination because it is not similarly situated to companies that have already entered markets and signed contracts with customers based on prior reciprocal-compensation rules. Instead CoreTel simply took the chance that it could continue to exploit this arbitrage opportunity despite being on notice at least "since the 1999 *Declaratory Ruling*" that such a gamble "might be unwise." *Order on Remand* ¶ 84. As the D.C. Circuit has made clear, the fact that CoreTel "sought to game the existing rules, and lost," provides no basis for a legal claim. *Global NAPs, Inc.*, 247 F.3d at 260. And, contrary to CoreTel's argument, the Commission's regime does not undermine its ability to compete for new customers against what CoreTel calls "incumbent CLECs." *See* Petition at 20-25. Those "incumbent CLECs" are essentially capped at the compensation they are receiving from *existing* customers and thus have no inherent advantage in obtaining *new* customers. In fact, in this regard, CoreTel is in at least as good a position as the ILECs, which have *never* been able to use reciprocal compensation windfalls to offer ISPs below-cost service, and have had to recover their costs from their own ISP customers.

In any event, CoreTel never comes to grips with the fact that the restrictions it challenges are part of a *transitional* mechanism that required the Commission to engage in line-drawing to account for competing regulatory goals. The Commission's "primary goal" in the *Order on*

Remand was to "address the market distortions under the current intercarrier compensation regimes." *Order on Remand* ¶ 77; *see id.* ¶ 74. The Commission also sought to accommodate a secondary goal. It determined that, in certain states that previously had imposed a reciprocal compensation requirement for Internet-bound traffic, "CLECs may have entered into contracts with vendors or with their ISP customers that reflect the expectation that the CLECs would continue to receive reciprocal compensation revenue." *Id.* ¶ 77. The growth caps and new-market restrictions reflect the Commission's attempt to create a regime that provides a transition for carriers that previously were entitled to such compensation, yet also moves rapidly to put an end to inefficient arbitrage opportunities.

CoreTel's argument here is nothing more than an attempt to second-guess the Commission's judgment as to the precise mechanism that should be used to accomplish those goals. CoreTel claims that, even though it was not providing service in certain markets, it is entitled to equal treatment with those who *were* providing service because, knowing that the issue was under review, it nonetheless chose to invest several hundred thousand dollars to enter those markets in the hope that it would receive reciprocal compensation for Internet-bound traffic. *See* Petition at 7-8. Consequently, CoreTel says that, because the Commission has decided to phase down reciprocal compensation payments for other carriers, payments to CoreTel effectively must be phased up. In other words, CoreTel asserts that the line the Commission has drawn to account for CLEC reliance interests is not perfectly calibrated to give it transition benefits that other, differently situated carriers, may derive. *See id.* at 23.

But the fact that a single party claims that a line the Commission has drawn for a temporary scheme is imperfect provides no reason to grant relief of any sort, much less the extraordinary relief of a stay. In fact, courts have repeatedly emphasized the leeway that this

Commission must be accorded in crafting transitional mechanisms. "Where the Commission drew the line amount[s] to a policy decision," and there is "no legal basis for concluding that some [other line] would clearly have been preferable" so long as the one chosen is a reasonable attempt to accommodate opposing concerns. *PSWF Corp. v. FCC*, 108 F.3d 354, 358 (D.C. Cir. 1997). Accordingly, as the D.C. Circuit recently held in directly analogous circumstances, the fact that a party claims unfairness from a bright-line rule provides no ground for relief where, as here, the Commission "balanced the need to implement the new regulatory regime against the effect of upsetting . . . expectations" and "reasonably feared" that adopting a different balance "would diminish the efficiency gains expected from" its new regime. *Bachow Communications, Inc. v. FCC*, 237 F.3d 683, 686-87 (D.C. Cir. 2001) (rejecting claims of discrimination raised by license applicants disadvantaged by the manner in which the Commission effectuated a transition from comparative hearings to competitive bidding; there was "no error in [the Commission's] resolution of the [] opposing interests").[2]

Indeed, even if CoreTel were correct that the interim scheme creates a minor, short-term market distortion in competition for new ISP business — which, for the reasons discussed above, it does not — the Commission was plainly acting within its discretion in finding it more important to eliminate the far larger "market distortions caused by the application of reciprocal compensation to ISP-bound traffic." *Order on Remand* ¶ 74; *see* Petition at 22; *see also Community Television, Inc. v. FCC*, 216 F.3d 1133, 1142 (D.C. Cir. 2000) (upholding transition

[2] CoreTel's suggestion that the Commission should have set CLEC-specific growth caps, rather than a uniform 10 percent cap, is likewise simply a claim that it falls on the wrong side of a line the Commission reasonably drew. *See* Petition at 24-25; *Order on Remand* ¶ 86. That is not a legitimate basis for the relief it seeks.

regime that disadvantaged some television licensees because the "agency reasonably balanced competing demands for spectrum"), *cert. denied*, 121 S. Ct. 761 (2001).

If all that were not enough, CoreTel's pleading itself makes plain that its claim depends in significant part on allegations of supposed misconduct by Verizon. *See* Petition at 3, 7-8. But CoreTel has already filed complaints to press those allegations, *see id.*, and its pursuit of those complaint proceedings, not a stay of the reciprocal-compensation order, is the appropriate mechanism for resolving its allegations. The Commission should not permit these carrier-specific disputes to become the tail wagging the industry-wide rulemaking dog.

Nor does CoreTel have a valid notice claim. *See id.* at 26-27. The possibility of a transition mechanism was fairly encompassed within the Commission's Public Notice, which sought comment generally "on a federal inter-carrier compensation mechanism for ISP-bound traffic" and requested that parties submit comments on "any new or innovative inter-carrier compensation arrangements for ISP-bound traffic."[3] Given the enormous financial stakes here, industry participants have long understood that such a new regime might well include a transition mechanism. Indeed, ALTS and CompTel, in the *ex parte* letter on which CoreTel here relies, expressly noted the "widespread recognition" that "a transition plan *would have to accompany* any such Federal intervention" into "the current compensation mechanism."[4] As those parties plainly understood, the Commission's interim compensation regime was well within the issues set for comment by the Public Notice or, at the very least, was a wholly lawful "logical

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[3] Public Notice, *Comment Sought on Remand of the Commission's Reciprocal Compensation Declaratory Ruling by the U.S. Court of Appeals for the D.C. Circuit; Pleading Cycle Established*, 15 FCC Rcd 11311, 11311 (2000). Notably, CoreTel overlooks this portion of the Public Notice. *See* Petition at 26-27.

[4] *Ex Parte* Letter from John D. Windhausen, Jr., ALTS, and H. Russell Frisby, Jr., CompTel, to Dorothy Attwood, Common Carrier Bureau, at 1 (Mar. 26, 2001) (emphasis added) ("ALTS/CompTel *Ex Parte*").

outgrowth" of the Commission's proposals and the comments it had received. *National Elec. Mfrs. Ass'n v. EPA*, 99 F.3d 1170, 1172 (D.C. Cir. 1996) (internal quotation marks omitted). Furthermore, "even if the agency has not given notice in the statutorily prescribed fashion," CoreTel's claim still fails because it is settled that "actual notice will render the error harmless." *Small Refiner Lead Phase-Down Task Force v. EPA*, 705 F.2d 506, 549 (D.C. Cir. 1983). CoreTel admits that a number of CLECs, as well as two CLEC associations, had actual notice of the Commission's plans to adopt a transition mechanism; notably, CoreTel itself never claims that it lacked such notice prior to the adoption of the *Order on Remand*. *See* Petition at 10-13.

Contrary to CoreTel's assertion, moreover, the Commission amply satisfied its procedural obligation to "respond in a reasoned manner" to significant comments. *Reytblatt v. Nuclear Regulatory Comm'n*, 105 F.3d 715, 722 (D.C. Cir. 1997). In fact, the Commission responded to every such comment raised in the various *ex parte* letters CoreTel cites. *See* Petition at 27-29. For example, ALTS and CompTel claimed that the growth cap would be discriminatory if it were based on 12 months of data because many newer CLEC switches would not have been in operation for a full year. *See* ALTS/CompTel *Ex Parte* at 3. The Commission responded by basing the cap instead on data from the most recent three months. *See Order on Remand* ¶ 78. Similarly, the Commission determined that competition between CLECs to serve existing ISPs, "not on the basis of the quality and efficiency of the services they provide, but on the basis of their ability to shift costs to other carriers," "undermines the operation of competitive markets," *id.* ¶ 71; that finding is fully responsive to claims that the growth cap discriminates against CLECs that seek to expand in just this manner. *See* ALTS/CompTel *Ex Parte* at 3; *Ex Parte* Letter from John T. Nakahata, Harris, Wiltshire & Grannis, to Magalie Roman Salas, FCC,

at 2 (Apr. 10, 2001) ("Level 3 *Ex Parte*").[5] Indeed, contrary to the misimpression CoreTel seeks to leave, ALTS, CompTel, and other CLECs actually *praised* the "reasonable compromise" that the Commission struck in the *Order on Remand*. *CompTel Views FCC Reciprocal Compensation Decision as a Victory for Competition and Consumers* (Apr. 19, 2001); *see, e.g.*, Statement of John Windhausen, Jr., ALTS (Apr. 19, 2001); Press Release, *XO Communications Issues Statement Regarding FCC Ruling* (Apr. 19, 2001).

2. The balance of equities here also counsels against granting a stay. In the first place, CoreTel can claim no right to uneconomic subsidy payments, and it has the same opportunity as incumbents to recover from its own ISP customers any costs it incurs. Consequently, CoreTel simply cannot show any legally cognizable injury.

Most important, the Commission has unequivocally established that the public interest is best furthered by taking "immediate action" to "eliminate [the] arbitrage opportunities presented by the existing recovery mechanism." *Order on Remand* ¶ 7. Those actions include the new-

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[5] Likewise, the *Order on Remand* responds to the claims of ALTS and CompTel that the rate caps must be set at CLECs' cost of carrying Internet-bound traffic (*Order on Remand* ¶¶ 76, 84); and that the Commission should not effectively impose bill and keep until it starts its industry-wide carrier compensation proceeding (*id.* ¶ 94). *See generally* ALTS/CompTel *Ex Parte*. The Commission also responded to Level 3's claim that it is not appropriate for the Commission to discourage CLECs from adopting business plans that target ISPs (*Order on Remand* ¶ 83) and Sprint's claim that rate caps are a sufficient response to the problems of reciprocal compensation for Internet-bound traffic (*id.* ¶¶ 76, 82, 86). *See* Level 3 *Ex Parte* at 2; *Ex Parte* Letter from Richard Juhnke, Sprint, to Magalie Roman Salas, FCC, at 1 (Apr. 16, 2001) ("Sprint *Ex Parte*"). Although the Commission did not directly address the "pooling" mechanism proffered, but not supported, by Level 3, or Sprint's support for "some sort of pooling mechanism," Level 3 *Ex Parte* at 2; Sprint *Ex Parte* at 1, the Commission did directly reject the premise of the pooling system: that the existing regime, under which carriers are compensated by other carriers rather than their end users, should be extended. *See Order on Remand* ¶ 81. The same analysis is found in the Commission's regulatory flexibility analysis, satisfying its obligation on that score. *See id.* ¶¶ 110-111; *ValueVision Int'l, Inc. v. FCC*, 149 F.3d 1204, 1212-13 (D.C. Cir. 1998).

market and growth-cap provisions of the interim compensation regime. *See id.* ¶ 77. Without those provisions, the expansion of compensation for Internet-bound traffic "would exacerbate the market problems we seek to ameliorate" and would "undermine our efforts to limit intercarrier compensation for this traffic." *Id.* ¶¶ 81, 86. Extending the ability of CLECs such as CoreTel to recover a significant portion of their costs from other carriers, rather than from their own customers, would further delay the "viable, long-term competition among efficient providers of local exchange and exchange access services" that both Congress and the Commission have sought to promote. *Id.* ¶ 71. Accordingly, even if this one carrier did have a legitimate interest that was harmed by the *Order on Remand*, that interest would be far outweighed by the powerful public interests that the Commission has already concluded are at stake here.

Moreover, incumbent LECs would also be irreparably harmed by a stay of the new-market and growth-cap provisions, because they would have to continue making enormous payments of reciprocal compensation on all Internet-bound traffic, thus diminishing their ability to compete in new and existing markets and to invest in new facilities. *See Order on Remand* ¶ 5 (under the prior regime, ILECs paid approximately $1.8 billion annually). The possibility that incumbents will not be repaid also creates irreparable harm. *See, e.g., Palmer v. City of Chicago*, 806 F.2d 1316, 1319 (7th Cir. 1986) ("To show irreparable harm it is enough to show that there was a danger . . . that the fees would disappear into insolvent hands."), *cert. denied*, 481 U.S. 1049 (1987).

CoreTel's asserted interests do not outweigh these significant private and public injuries. Indeed, CoreTel's own actions in this proceeding — namely, its unexplained 35-day delay before seeking "emergency relief" from an order that would allegedly "force [it] out of business" in nearly half of its markets, Petition at 6 — belie any claim that it will suffer irreparable harm in

the absence of a stay. *See, e.g., Tough Traveler, Ltd. v. Outbound Prods.*, 60 F.3d 964, 968 (2d Cir. 1995); *Citibank, N.A. v. Citytrust*, 756 F.2d 273, 276-77 (2d Cir. 1985). Indeed, because CLECs "have been on notice since the 1999 *Declaratory Ruling* that it might be unwise to rely on the continued receipt of reciprocal compensation for ISP-bound traffic" (*Order on Remand* ¶ 84) any harm that CoreTel faces is a product of its own unwarranted reliance on a compensation regime scheme it had every reason to know might end at any time. *See* Petition at 8. And, for the reasons discussed above, CoreTel is wrong in asserting that the Commission's scheme prevents it from competing with other CLECs for new customers. But even if it were right on that point, the only response that would be consistent with the principles announced in the *Order on Remand* would be to end reciprocal compensation immediately for all CLECs, thus ensuring CoreTel of the level playing-field it claims to seek. CoreTel notably fails to suggest such a remedy for its alleged competitive injuries.

CONCLUSION

For the foregoing reasons, the Commission should deny CoreTel's motion for a stay.

Respectfully submitted,

/Mark L Evans/SAL

MARK L. EVANS
SEAN A. LEV
SCOTT H. ANGSTREICH
KELLOGG, HUBER, HANSEN, TODD
& EVANS, P.L.L.C.
1615 M Street, N.W.
Sumner Square
Suite 400
Washington, D.C. 20036
(202) 326-7900

Counsel for BellSouth Corporation, SBC Communications Inc., the Verizon telephone companies, and the United States Telecom Association

JAMES G. HARRALSON
BELLSOUTH CORPORATION
1155 Peachtree Street, N.E.
Suite 1800
Atlanta, GA 30309
(404) 249-2641

Counsel for BellSouth Corporation

ROGER K. TOPPINS
GARY L. PHILLIPS
SBC COMMUNICATIONS INC.
1401 I Street, N.W.
Suite 1100
Washington, D.C. 20005
(202) 326-8912

JAMES D. ELLIS
PAUL K. MANCINI
SBC COMMUNICATIONS INC.
175 E. Houston
San Antonio, Texas 78205
(210) 351-3500

Counsel for SBC Communications Inc.

MICHAEL E. GLOVER
EDWARD H. SHAKIN
JOHN M. GOODMAN
VERIZON
1320 North Courthouse Road
8th Floor
Arlington, VA 22201
(703) 974-4862

Counsel for the Verizon telephone companies

LAWRENCE E. SARJEANT
LINDA L. KENT
KEITH TOWNSEND
JOHN W. HUNTER
JULIE E. RONES
1401 H Street, N.W., Suite 600
Washington, D.C. 20005
(202) 326-7371

Counsel for United States Telecom Association

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CERTIFICATE OF SERVICE

I, Tara M. Brooks, hereby certify that on this 8th day of June 2001, I served a true and correct copy of the foregoing Opposition of BellSouth Telecommunications Inc., SBC Communications Inc., the Verizon Telephone Companies, and the United States Telecom Association to Petition of Core Communications, Inc. for Stay Pending Judicial Review upon the following via hand delivery:

Core Communications

Glenn B. Manishin
Stephanie A. Joyce
Patton Boggs LLP
2550 M Street, N.W.
Washington, D.C. 20037

John T. Nakahata
Timothy J. Simeone
Harris, Wiltshire, & Grannis LLP
1200 Eighteenth Street, N.W.
Washington, D.C. 20036

Federal Communications Commission

Dorothy Attwood
Tamara Preiss
Glenn Reynolds
Jane Jackson
Common Carrier Bureau
Federal Communications Commission
445 12th Street, S.W.
5th Floor
Washington, D.C. 20554

Jane Mago
Laurence Bourne
John Ingle
Ted Olson
Jane Jackson
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Tara M. Brooks